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Offshoring: Where's the value?

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U.S. firms that offshore customer service may save money on labor costs, but they also pay the price in terms of unhappy customers, say University of Michigan researchers.

"Firms are increasingly offshoring front-office functions such as customer service call centers and back-office functions such as information technology to manage their operations and achieve their strategic objectives, including expansion to new markets, access to global talent or improved efficiency," said M.S. Krishnan, professor of business information technology at Michigan's Ross School of Business.

"However, the implications of offshoring from a customer perspective may differ depending on the functions that are offshored."

Krishnan and colleagues Claes Fornell of the Ross School and Jonathan Whitaker of the University of Richmond analyzed the offshoring and outsourcing activities of 150 North American firms and business units from 1998 to 2006. They used Fornell's American Customer Satisfaction Index to measure customer satisfaction and gleaned over 50,000 news reports for information on the offshoring and outsourcing activities of firms.

The researchers found that offshoring and domestic outsourcing of front-office (customer service) functions result in similar declines for customer satisfaction. Prior work shows that the average ACSI decline is associated with a drop of 1 percent to 5 percent in a firm's market capitalization, depending on the industry.

Other surveys show that nearly nine in 10 American customers have experienced some kind of problem when contacting overseas call centers, including lack of responsiveness, reliability and other variables of service quality.

"With the cultural, language, distance and time-zone differences inherent in offshore services, one or more of the (service quality variables) may not translate properly in the offshore service setting," said Fornell, professor of marketing at Michigan's Ross School of Business.

However, when it comes to offshoring back-office functions (information technology, human resources, finance and accounting, and research and development), there is no decline in customer satisfaction.

Overall, the researchers suggest three primary implications of their study.

"Firms must carefully consider which functions are suitable for offshoring and they must ensure that their overseas vendors are properly equipped to provide high-quality service to customers," said Whitaker, assistant professor of management at the University of Richmond's Robins School of Business. "Finally, in addition to using offshoring as an opportunity to save on internal costs, firms must also use offshoring as an opportunity to create additional value for customers."

The researchers say that, as a starting point, firms should invest some of the savings from offshoring to serve customers they previously could not afford to serve, or to provide additional services to current customers. As a next step, firms can use offshoring to access additional innovation in the marketplace for global resources and pass these innovations on to their customers.

At any rate, Krishnan, Fornell and Whitaker say that offshoring activities of American firms can be successful if the process is properly managed.

"Firms may have a limited and short-term perspective in their initial decision to outsource—onshore or offshore—based on internal business process performance," Krishnan said. "Our research enables firms to account for customer perceptions in making their decision and facilitates a more a comprehensive approach to the decision process for offshoring and outsourcing."

Source: University of Michigan